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SOURCES OF REVENUE

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Real Estate Tax. The backbone of the revenue system of American cities is the tax on real estate. In the average city the tax levy on ordinary land and buildings is more than four-fifths of the general tax levy and yields more than half of the total revenue. These proportions, of course, vary in different cities. In Augusta, Georgia, for instance, the levy is but three-fifths of the general levy and yields only one-fourth of the total revenue. In New York, on the other hand, the levy on ordinary land and improvements constitutes nine-tenths of the total property levy and produces two-thirds of the entire revenue.

As the real estate tax is the most important source of revenue, the method of its assessment and levy merits the most serious attention. The scientific assessment and taxation of real estate is obviously the first step to be taken by a city in any attempt to improve its financial condition.

Limitations on Tax Rate. The tax rate should always be fixed by budgetary requirements, not by statute. If the fixed tax rate is larger than that required by a city, it will result in extravagance and waste. If it is too small, it will result in the throttling of necessary expenditure; or in the tapping or retention of undesirable sources of revenue; or in the borrowing of money for current account. A congressional committee recommended the repeal of the fixed tax rate in Washington in 1912.

A limited tax rate is only less harmful than a fixed tax rate. The cities of Ohio are at present having serious financial difficulties on account of the statutory limitations imposed on the tax rate. The limitations on the tax rate in Massachusetts were found so ineffective in their design and so irksome in their operation that they were repealed in 1913. The only city in the state that has a limited tax rate at present is Boston.

Semi-Annual Collection of Taxes. Taxes should be collected semi-annually, the first installment at the commencement of the fiscal year and the second six months later. This policy has three advantages: (1) it effects a large saving in the interest paid on temporary loans issued in anticipation of taxes; (2) to the extent that such loans are reduced the market for long term borrowings is improved,—the capital available for investment in city bonds is increased; (3) it diminishes tax delinquencies by permitting property owners, unable to pay their whole tax, to pay half and to go into arrearage for the other half.

Tax Discounts. No discount should be allowed for the payment of taxes. The best way to secure prompt payment of taxes is to charge a high interest rate on those remaining unpaid after a fixed date. If a discount is granted, the tax budget will have to contain an appropriation equal to the amount of the discount. If all taxpayers could take advantage of the discount to the same extent, the result would be nil—the rebate allowed each property owner would exactly offset the amount of his additional tax. But all property owners cannot avail themselves of the discount. The result is that the taxpayers availing themselves of it are favored with a differential tax rate at the expense of those who don't.

Full Value Assessments. All real estate should be assessed at full value. With true value as the basis of assessment, over-assessments and underassessments are more apparent and, therefore, more easily corrected. An accurate assessment based on a percentage of true value entails a greater amount of work on the assessor than a full value assessment. He must first ascertain the full value and then proceed to calculate the percentage of assessment. A full value assessment saves this computation.

Assessment at part value, moreover, gives a low tax rate the appearance of a high one. This artificial stimulation of the tax rate results either in the non-performance of much necessary work, or in its payment out of borrowed money when it should really be charged to current revenue. The borrowing power of cities has as a consequence of this policy been seriously abused. When assessments are at, say 20 per cent of true value, as they are in many cities, the temptation to borrow for current purposes is almost irresistible. A 1 per cent levy on true value when translated into terms of a rate on such an assessment becomes a 5 per cent tax.

Annual Assessments. Assessments should be made annually, not biennially or triennially. An annual assessment of real estate greatly improves the administration of the assessing department. The assessors being practically the whole time in the field become experts in valuation. This secures uniformity of assessment. The annual assessment of real estate, moreover, increases the revenue of a city in that the increment in land value is intercepted every twelve months instead of every two or three years. It is also true that if real estate is not assessed annually, land of a declining value will be over-assessed a large part of the time. Biennial and triennial assessments necessitate large and abrupt increases in the assessment of property rising in value. This excites much dissatisfaction among owners. Annual assessments to a large extent overcome this difficulty in that the increases are smaller and more gradual.

Separate Assessment of Land and Buildings. It is most important that land and buildings be assessed separately. Unless this is done a scientific assessment of real estate is impossible. Land tends to appreciate in value; buildings to depreciate. This fact makes it necessary to assess the two by different standards. To value both together inevitably results in an unequal assessment of property.

Not more than half of the cities with a population exceeding 30,000 assess buildings and land separately.

In the cities that do make separate assessments the greatest divergency is found in the per capita land and building values. Taunton, for instance, has a per capita land value of only \$147. San Diego has a per capita land value of \$2,130. In Manhattan the per capita land value is \$1,258, and in New York as a whole only \$840. In Atlantic City it is \$1,089; in Los Angeles, \$1,100; and in San Francisco, \$1,380. These cities illustrate the extreme. In the average city it is less than \$400.

The assessed building value per capita ranges from \$140 in Perth Amboy to \$750 in Newton. In the average city it is between \$300 and \$500.

Methods of Assessment. An improved parcel scientifically assessed will usually not be assessed at a higher figure than its capitalized rental unless the land value alone exceeds this sum. Its assessment, moreover, will ordinarily not be raised on account of an

increasing land value, except where such increased value results in a larger rental.

No building should be assessed at more than the difference between the value of the land and the aggregate value of the land and building. The value of new buildings should be computed by applying appropriate factors of value per square foot of floor space to the entire floor surface. The factor chosen in any particular case should be adjusted among other things with reference to the kind of building, the height between floors, the state of depreciation and obsolescence, and the per cent of lot area covered.

Land Value Maps. Land value maps should be published annually. These maps show the value per front foot of inside lots on grade and of standard depth on each side of every block in the city. In the case of unplotted land they show the acreage value. Maps of this character aid: (1) the assessor in making equitable assessments by presenting him with a view of all his territory with comparable figures on every street; (2) the board of review in passing upon applications for a reduction of assessments; and (3) the public in judging the fairness of the assessments.

Land value rules should be utilized in computing the assessments of lots of irregular depth and shape. Such rules are used by Cleveland, Newark and New York.

Tax Maps. Tax maps showing the boundaries and dimensions of every lot are indispensable to an accurate assessment of land. Without their aid it is impossible to be certain whether all real estate has been assessed. Where they are not used considerable property escapes all assessment and taxation.

Tax maps are not found at present in most of the smaller cities and towns.

Exemption of Buildings. There is a movement on foot in many cities at present to exempt improvements from taxation. The policy has so far been adopted in part by only two cities, Pittsburgh and Scranton.

Exemption can be most readily effected in cities with a rapidly increasing land value and a small improvement value as compared with the total real estate value. Given this condition the untaxing of buildings would mean only a slight increase in the present tax rate on land values and this could be done without seriously inconveniencing either the city's finances or private property rights.

This is especially true of such western cities as Berkeley, Los Angeles, Oakland, Sacramento, San Diego, San Francisco, Seattle, Spokane and Tacoma. In all these cities the assessed land value is almost double or more than double the assessed improvement value. In San Diego for instance, improvements are assessed at but 17 per cent of the total real estate. The land tax, therefore, produces almost five times as much income as the building tax. The improvement levy yields less than 8 per cent of the total municipal revenue. The land levy yields 35 per cent of the total revenue. San Diego is, however, an extreme case. In the other cities named above the improvement levy yields from 15 to 20 per cent of the total revenue, and the land levy from 30 to 40 per cent of the total revenue. It is doubtful whether any city in the United States derives less revenue from the taxation of improvements than San Diego. This city is, therefore, the logical place in which first to exempt improvements from taxation. In no city, however, do land values contribute a greater share of the total revenue than in New York. That city derives 41 per cent of its total revenue from the tax on ordinary land values. The tax on improvements contributes 25 per cent of the total income.

The relation of land value to total real estate value varies enormously in different cities. Generally speaking it fluctuates between one-third and one-half of the real estate value. But in Chelsea, Everett, Pawtucket, Taunton, West Hoboken, and Woonsocket, the assessed improvement value is twice or more than twice the assessed land value. Taunton, for instance, derives only 11 per cent of its revenue from the taxation of land values while it derives 25 per cent from the taxation of building values. West Hoboken, Chelsea, Woonsocket, and Everett derive 13, 15, 17 and 19 per cent of their revenue respectively from the taxation of land values; and 29, 30, 34 and 38 per cent respectively from the taxation of improvement values.

Cities deriving such a large percentage of their revenue from improvements would obviously have great difficulty in exempting them from taxation. Exemption wherever effected will, as a rule, have to be very gradual or the municipal finances will be seriously embarrassed.

Special Assessments. Some cities derive as much revenue from special assessments as from the general property tax. They are

most freely resorted to in western cities. There the limitations on the debt incurring power are frequently so stringent as to render loans for improvements impossible and the tax limit so low as to make their payment out of the tax budget out of the question.

Assessment of Street and Park Openings. Any public improvement conferring a local benefit should be assessed. The assessment should be limited only by the cost of the improvement and the amount of benefit. No part of the cost should be assumed by the city where the local benefit is sufficient to pay the whole expense.

Assessments for street openings are more general than those for park openings. In the acquisition of parks, however, Kansas City assesses the entire cost. Denver, Indianapolis, and Minneapolis assess a substantial part of the cost. Before 1855 it was the practice in New York to assess the entire cost of park openings. During the next twenty-five years from one-third to one-half of the cost was assessed. Since 1880 the city has assumed practically the entire cost. Only within the last few years has an attempt again been made to assess the cost of parks.

The best procedure governing assessments for street openings is probably found in New York.¹ The Board of Estimate and Apportionment has the power to fix the benefit area. The benefits may be apportioned between districts of special benefit, one or more boroughs, or parts of boroughs, and the city at large. Levies against one or more boroughs or the city at large are in the nature of flat rate assessments and collected with the annual real estate tax. The rules controlling the benefit area and the apportionment of assessments in street openings are most elaborate. Lack of space forbids a detailed account of them here.

Assessment of Physical Improvements. The cost of local improvements, pavements, sidewalks, water and sewer mains, etc., should be assessed only in those cases where the work adds to the city's capital account. In other words such assessments should be limited to the original improvement unless a subsequent improvement is of a higher standard than the original. Then the cost of the subsequent improvement, in so far as it is of a superior grade than the first, might be assessed.

Only the first improvement confers a local benefit; the subse-

¹ Nelson P. Lewis, *Paying the Bills for City Planning*, Proceedings, Fourth National Conference on City Planning, 1912.

quent improvements, unless they are of a better quality, merely maintain the benefit conferred by the first. If this principle is not acted upon, assessments for local improvements will in effect have to be made a regular source of city revenue. This would be most unfortunate. It would result, as it were, in the creation of as many special taxing districts as there are separate improvements. The land values in the central part of the city are due quite as much to the activities of the people living in the suburbs as to those living in the heart of the city. It is consequently only just and fair that the cost of subsequent improvements should be provided for in the annual budget. In a large city the amount of work required each year is fairly regular. Its payment in this manner would consequently not impose any greatly fluctuating charge on the tax rate.

To have the contractor act as the collector of assessments increases the cost of improvements as in making his bid he must discount the probability of the less valuable properties being unable to bear their assessments.

The contractor should be paid during the construction of the improvement as the work progresses. To defer payment until the improvement's completion obliges the contractor to include an added amount for interest charges in his bid. This practice also reduces competition for city work. Contractors unable to command sufficient credit to finance the work to its completion are eliminated from the bidding.

Payment should be made, not in warrants or assessment bonds, but in cash. Paper issued to contractors is usually not sold at par. The amount of discount, which varies from 5 to 10 per cent, is, of course, added to the prices bid.

The maintenance of a revolving fund, replenished by assessments as they are collected, is probably the best method to enable the city to pay cash for its physical improvements.

Excess Condemnation. Every city should acquire the right of excess condemnation in undertaking public improvements, especially in the laying out of new streets and in the widening or extension of old ones.² The financial advantage that will accrue to the city from the exercise of this right will be found quite as much in the

² For an exhaustive discussion of excess condemnation see the report prepared by the present writer for the National Municipal League, and published by the New York Committee on Taxation, 1915.

increase of the taxable values due to the economic replotting of areas adjacent to such improvements as to the profits derived from the resale of surplus land. The land adjacent to a street is generally divided into plots the shape and size of which are adapted, as well as might be to the street's present use and condition. Widening a street, or laying out a new one in a built-up quarter disturbs this equilibrium. Not only are the existing buildings destroyed, but the abutting lots, after the work's completion, are frequently left so distorted in shape and so diminutive in size as seriously to impair, if not utterly to destroy, the proper use and development of the thoroughfare. For such a street to attain its natural importance it is necessary that the land fronting upon it should be wholly rearranged and replotted.

There are many instances in our cities where street improvements have appropriated all but ten or twenty square feet of large lots. Remnants of such size are not only useless themselves, but they also keep other lands to the rear of them from being utilized to their best advantage. The present practice in making street improvements instead of enhancing the values of adjacent land frequently militates against its best economic use as actually to depreciate the taxable values.

Under excess condemnation, the city might, in addition to the land requisite for a thoroughfare, appropriate these small parcels, obliterate the existing lot lines, and replot the frontages of the street in a manner conducive to its most wholesome development. The city would be in a far better position than the private owners to replot these injuriously affected plots. The cost, moreover, of acquiring the additional land would be negligible. When so much of a lot has to be taken as to leave the remainder practically worthless, the price that must be paid for the appropriated part is, as a rule, as great as the market value of the whole.

New York, Massachusetts, Ohio and Wisconsin have adopted constitutional amendments to enable their cities to exercise excess condemnation.

The Unearned Increment Tax. The unearned increment tax is the most fruitful new source of revenue that can be adopted.³

³ For a more complete discussion of this tax see the article by the present writer, entitled "The Unearned Increment Tax," in the *National Municipal Review*, April, 1914.

The scheme worked out by the New York Commission on New Sources of City Revenue for the taxation of the unearned increment is at once a model of simplicity and applicability to American conditions.

Briefly stated, this plan proposed to assess and tax annually all increment accruing in the future in the same manner as existing site values are now assessed and taxed. No heed is paid to sale or transfer of title in the imposition of the tax. The site value, as determined by the assessor for the year the tax goes into effect, is made the standard by which to measure all future increment, the assumption being that the valuations fixed by this department fairly reflect the current market values. Taxation of the increment in no wise exempts or relieves a parcel from payment of the ordinary real estate tax, the new tax being an addition thereto, although imposed only on that portion of the site value accumulated after the basic year.

If the assessed site value of a parcel, for instance, should be increased \$10,000 above the assessment of the basic year, the owner would pay an annual surtax on the amount of this increment in addition to the regular tax on the total value of his site.

Increment arising from improvements, such as grading, sewerage, paving, etc., the cost of which has been borne by the owner, is, to the extent of such cost, deducted from the increment assessed. The increment assessed in any particular year is, therefore, the difference between the site value assessment for that year and the site value assessment for the basic year, after deducting the cost of improvements made during the interim. To illustrate: if the value of a piece of land should rise from \$100,000 in the basic year to \$110,000 after the basic year, and the owner could show that he had spent \$4,000 in permanent improvements, either upon his own initiative or in payment of special assessments levied by the municipality, he would be taxed on an increment of only \$6,000; and the base value of the land for the future assessment of increment would thenceforth be \$104,000 instead of \$100,000.

Examined from every point of view, the tax recommended by the Commission on New Sources of City Revenue is an infinite improvement over the English or German method of taxing the increment in site values. It differs most radically from the tax in either of these countries. In England and Germany the state in

consideration of a lump sum payment parts forever with its right to appropriate these unearned values. Under the suggested plan the state would retain a rent charge in perpetuity on all increment.

As a revenue measure, the proposed tax has a vast advantage over the English or the German tax. As applied in these countries the revenue produced by the tax is almost entirely dependent upon the real estate market, and, therefore, subject to the most violent fluctuations.

The tax recommended by the commission would produce a revenue which in its amount would be easily calculable from year to year. Its yield, moreover, in addition to being steady, would increase in amount. The Department of Taxes and Assessments estimates that site values in New York City increase at the rate of 4 per cent per annum. The proposed increment tax at a rate of 1 per cent would reduce this increase to about $3\frac{1}{2}$ per cent. Assuming this rate of increase to continue, the proposed tax would in thirty-two years yield a revenue equal to a 2 per cent tax on the present assessment of ordinary land values.

Personal Property Tax. The personal property tax should be abolished. In some cities this could be done immediately without any great financial inconvenience. Personal property in New York, for instance, constitutes only 3 per cent of the general property assessment and yields only 2 per cent of the total revenue. Most cities, however, derive a much larger income from personal property. the levy in such cities as Chicago, Cincinnati, Cleveland, Detroit, and Minneapolis, constitutes between 25 and 35 per cent of the total general property levy. In these cities the abolition of the tax would probably have to be effected very slowly.

No increased revenue is to be expected by taxing personalty at a low rate. The experience of Connecticut, Iowa, and Minnesota proves this.

Business Taxes. The imposition of business taxes as a source of revenue is not to be commended. If large in amount they are apt to affect the business of a city most unfavorably, even to the extent of completely driving it away. They are also undesirable in that they confer a monopoly advantage upon those able to pay the tax by rendering certain businesses inaccessible to the poorer classes.

Licenses. Licenses should be confined to such businesses as require inspection and regulation under the police power. The

cost of necessary supervision should fix the amount of the fee charged. A fee in excess of the cost of regulation would be very much in the nature of a tax.

Permits, Privileges and Concessions. All permits, privileges and concessions should as a general rule be let at public auction. No free privileges should be granted. The fee should be of a fixed amount and collected periodically. It should not be based on the net or gross receipts of the business. This plan has been tried in different cities and is thoroughly discredited. A city to administer it successfully would have to employ a large staff of accountants and detectives.

Departmental Fees. Fees charged for departmental services should not exceed the amount necessary to make their respective departments self-sustaining.

Municipal Enterprises. Municipal enterprises, waterworks, electric light plants, gas plants, etc., should not be operated for profit. The rates charged should conform to the cost of service, including of course, the interest and amortization charges. To charge more than this results in unequal and inequitable taxation.